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Supreme Court of the United States

OCTOBER TERM, 1946

No. 42
No. 43

IN THE MATTER
of
AMERICAN FUEL & POWER COMPANY, INLAND GAS CORPORATION,
KENTUCKY FUEL GAS CORPORATION,
Debtors.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,
against
LOUIS A. GREEN and ROBERT HEILBRUNN, Known in these Proceedings as the GREEN COMMITTEE and MORRIS GREEN,
Respondents.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,
against
CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, JACK PATTON and P. G. MEADOR,
Respondents.

PETITION FOR REHEARING

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PETITION FOR REHEARING

Petitioners respectfully suggest that the Court has overlooked certain basic facts, and that applying the principles stated in the opinion to those facts, a reversal of the judgment of the Circuit Court of Appeals is required.

1. Extent of the Lien

Initially, we point out the nature and extent of the mortgage lien of the Inland First Mortgage bondholders. The mortgage securing the Bonds was held to cover everything the corporation owns (Finding II and Conclusion of Law VI of the District Court, R. 193). Respondents objected to this holding and claimed on appeal that the mortgage did not cover (1) income earned before the filing of the mortgage foreclosure bill in the equity receivership, (2) cash on hand at the time of the appointment of the equity receiver on a creditor's bill and (3) after-acquired property. The Circuit Court of Appeals held against Respondents on all these points. (R. 229-234), 151 F. (2d) 470, 480-483 (1945).

Petitioners seek to enforce their contractual right to interest on interest coupons only out of the mortgaged property. A bondholder "may look to his lien not only for the principal but also for interest accruing up to the date of payment, though his debtor has gone into bankruptcy (*Coder* v. *Arts*, 213 U. S. 223, 245, affirming, 152 Fed. 943, 950) or into equity receivership (*American Iron & Steel Mfg. Co.* v. *Seaboard Air Line Ry.*, 233 U. S. 261), and though interest will be denied the unsecured creditors if the assets are insufficient to pay all claims in full". *Ticonic Bank* v. *Sprague*, 303 U. S. 406, 413 (1938). As the quotation by the Court from *Group of Investors* v. *Milwaukee*, 318 U. S. 523, 573 (1943), shows, it is only in those instances in which the secured property is less than the amount of the secured creditor's total claim that interest above the amount of the security is disallowed. See also *Sexton* v. *Dreyfus*, 219 U. S. 339 (1911).

2. The Equities

Only on the assumption that the mortgage does not cover all the debtor's assets do we, as the Court states, "make a balance of equities between creditor and creditor or between creditors and the debtor". Balancing these equities

we find the scales weigh heavily in petitioner's favor. Over a number of years subsequent to 1930 the interest requirements on the bonds were not earned, but from about 1936 on, with some ups and downs, there was a marked improvement in gross earnings. (R. 73, 75, 77, 79, 81, 82, 83.) When in 1943 the instant question arose on an application for a distribution, the balance sheet showed a decided change obviously due to the production and sale since 1930 of the mortgaged gas. Current assets there appear at about $2,800,000 (R. 168-169). We believe the Court need only assume what is the fact, but not of record, that with existing business conditions the average earnings since 1943 have continued at not less than the rate of the latest three years shown in the record, *i. e.* roughly $370,000 per year, in order to come to the conclusion that there are now assets sufficient, if its decision stands, to make a payment on the stock of the Debtor.*

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* The record (paragraph Sixth of the Application for distribution, R. 167) shows that the rejected claims of Columbia Gas & Electric Corporation, of about $2,160,000 principal amount are included in the balance sheet liabilities (R. 169), and this rejection has been upheld on appeal. *Columbia Gas & Electric Corporation* v. *U. S.*, et al., 151 F. (2d) 461 (1945) certiorari denied, 67 S. Ct. 48 (1946). If the claims of Columbia, including interest, computed by the Trustee at $3,514,847.48 on June 30, 1943, are eliminated the earned surplus item $6,654,586.38 (a red ink figure R. 169) is decreased to $3,139,738.90. If capital stock shown on the same page at $2,126,587 is deducted from this latter amount we have a red surplus figure of $1,013,151.90.

The average earnings for 1941, 1942 and 1943 are roughly $370,000 a year (see "net income" items, R. 82, 83, 84, after adding thereto unpaid interest on funded debt). Assuming this rate continued through 1944-1946 the Company is now $1,100,000 better off, and this amount wipes out the above red surplus figure of $1,013,151.90 and leaves something for the stock. Actually in 1944 the net income before interest on funded debt was approximately $517,000; in 1945 approximately $475,000 and for the first half of 1946 approximately $280,000. The Trustee advises net income for 1946 will exceed that for the year 1944, making an aggregate for the three years of approximately $1,500,000.

If it be claimed that the fixed capital is a wasting asset with little future return, we call attention to the fact that in the period 1941-1943 depreciation, depletion and amortization averaged

In the early stages of the proceedings there was little if anything out of which interest could be paid on the bonds, and nothing was paid them, but instead, at their expense, the avails of the property were plowed back and were used to build up a very satisfactory financial position for the estate. This increase in the earnings and assets points up the inequity of disallowing interest on interest coupons to the unjust enrichment of junior creditors and stockholders.

The basic rationale of the Court's opinion is that it is inequitable for one class of creditors to gain an advantage or suffer a loss *vis-a-vis* another class from the delay which is the inevitable result of the preservation of the debtor's estate for the benefit of all interests. See *Sexton* v. *Dreyfus, supra*, 346; *American Iron Co.* v. *Seaboard Air Line*, 233 U. S. 261, 266 (1914). Thus claims of various classes are retained in the same proportion as at the time of the filing of the petition, as if "the whole matter could be settled in a day by a pie-powder court." *Sexton* v. *Dreyfus, supra*, 344-345; *Ticonic Bank* v. *Sprague, supra*, 411. Should over the years the estate diminish or remain static the senior class may well benefit disproportionately to the junior classes if interest be paid. On the other hand quite the opposite result follows in a case such as this where the estate has increased. This is the holding of Mr. Justice Holmes in *Sexton* v. *Dreyfus, supra*. In allowing earnings after the date of the petition to be applied to interest accruing after such date, he stated: "There is no more reason for allowing the bankrupt estate to profit by the delay beyond the day of settlement than

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$208,813.69 a year (R. 82-84) and the balance sheet as of June 30, 1943 (R. 168-9) shows the gas plant, after depreciation, depletion and amortization, to have a value of approximately $2,900,000. It should be noted that the amount of depreciation, depletion and amortization for the years 1931-1940, averages $236,278.51 (R. 73, 75, 77, 79, 81) which would indicate, what is the fact but not of record, *i. e.*, the acquisition of new gas reserves by the Trustee at a low figure and the abandonment of useless reserves carried at a high figure, all pointing to a favorable future for the properties.

there is for letting the creditors do so". Here the junior creditors and the stockholders profit from the inevitable delay which is no fault of the senior creditors,* and the senior creditors are subjected to a grievous loss. Had they obtained their share of the assets, that is, one hundred per cent, as of the inception of the proceedings, the entire increase in value of the estate would have accrued to them outside bankruptcy. To deny them a part of this increase in the form of interest on interest coupons is to place upon them the entire risk of a diminution of assets with no compensating advantage and is an inducement to junior creditors to delay winding up.

The ordinary conception of interest as compensation for the use of money (see *Ticonic Bank* v. *Sprague, supra,* 411; *Old Colony R. Co.* v. *Comm'r,* 284 U. S. 552, 560 (1932); *Deputy* v. *DuPont,* 308 U. S. 488, 498 (1940); *Equitable Society* v. *Comm'r,* 321 U. S. 560, 564 (1944); *John Kelley Co.* v. *Comm'r,* 326 U. S. 521, 530 (1946)), is an expression of the above principles. Basically in the business world interest presupposes that the money loaned will be used to profit and advantage and that therefore compensation should be paid for its use. Only when no profits are made by the borrower does interest resemble in any way a penalty. That is not this case. Here the debtor's estate has made extraordinary profits.

Under the carefully drawn and, as the Court assumes, valid covenant (R. 203-4) the interest in question should be given that "absolute priority" over stockholders it would have if the question had arisen on the approval of a plan of reorganization. *Consolidated Rock Co.* v. *DuBois,* 312 U. S.

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* That the delay in this case has been inevitable and no fault of the First Mortgage bondholders is apparent from the reported cases. Claims amounting to many millions of dollars have been denied preference and the Columbia claims have been eliminated. *In re Inland Gas Corporation,* 91 F. (2d) 113 (1937); *Hamilton Gas Co.* v. *Inland Gas Corporation,* 102 F. (2d) 131 (1939); *In re American Fuel & Power Co.,* 122 F. (2d) 223 (1941); *Columbia Gas & Electric Corporation* v. *United States,* 151 F. (2d) 461 (1945).

510, 527-8 (1941); *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, 116-7 (1939).

Furthermore, we believe a coupon is uniformly considered a negotiable instrument and, in a sense, a special type of interest which ordinarily can be sued on separately, and, when judgment is obtained, interest accrues from the due date of the coupon. Cf. New York Code of Civil Procedure, Section 480. *Central National Bank* v. *Bateman & Co. Inc.*, 15 Del. Ch. 31, 131 Atl. 202 (1925); *Bowman* v. *Neeley*, 137 Ill. 433, 27 N. E. 758 (1891); 151 Ill. 37, 37 N. E. 840 (1894); *Abbott* v. *Stone*, 172 Ill. 634, 50 N. E. 328 (1898); *Kentucky Title Company* v. *English*, 20 Ky. L. Rep. 2024, 50 S. W. 968 (1899); *Pensacola & A. R. Co.* v. *Hilton's Trustee*, 147 Ky. 553, 144 S. W. 1077 (1912).

We believe the facts of record indicate that the overwhelming balance of equities is in favor of petitioners. The full record in this insolvency further emphasizes that balance. We respectfully suggest that if the Court does not desire to grant a rehearing, then in the interests of a fully informed judgment, *Consolidated Rock Company* v. *DuBois, supra*, 520, the case be remanded to the District Court for a complete hearing on the equities.

December 31, 1946.

Respectfully submitted,

GEORGE W. JAQUES,
Counsel for Petitioners,
Vanston Bondholders
Protective Committee.

Certificate of Counsel

I, GEORGE W. JAQUES, attorney and counsel herein for the Vanston Bondholders Protective Committee, do hereby certify pursuant to Rule 33 that the foregoing Petition for rehearing is presented in good faith and not for delay.

December 31, 1946.

(S) George W. Jaques